Internal Revenue Service

memorandum

date:

to: District Director
[redacted] District

from: Assistant Chief Counsel
(Employee Benefits and Exempt Organizations)

subject: Taxation of Employer-Provided Helicopter Flights

This memorandum is in response to your request for guidance regarding the income tax consequences to Governor [redacted] in connection with flights he has taken using a helicopter provided by the State of [redacted].

Section 61(a)(1) of the Internal Revenue Code provides that gross income means all income from whatever source derived, including (but not limited to) compensation for services, including fees, commissions, fringe benefits, and similar items.

Section 132(a)(3) of the Code provides that gross income shall not include any fringe benefit which qualifies as a working condition fringe.

Section 132(d) of the Code provides that the term "working condition fringe" means any property or services provided to an employee of the employer to the extent that, if the employee paid for such property or services, such payment would be allowable as a deduction under section 162 or 167.

Section 1.132-5(a)(1)(ii) of the Income Tax Regulations provides that if, under section 274 or any other section, certain substantiation requirements must be met in order for a deduction under section 162 or 167 to be allowable, then those substantiation requirements apply when determining whether a property or service is excludable as a working condition fringe.

Section 1.132-5(a)(2) of the regulations provides that if the hypothetical payment for a property or service would be allowable as a deduction with respect to a trade or business of an employee other than the employee's trade or business of being an employee of the employer, it cannot be taken into account for purposes of determining the amount, if any, of the working condition fringe.

Section 1.132-5(c)(1) of the regulations provides that the value of property or services provided to an employee may not be excluded from the employee's gross income as a working

condition fringe, by either the employer or the employee, unless the applicable substantiation requirements of either section 274(d) or section 162 (whichever is applicable) and the regulations thereunder are satisfied. The substantiation requirements of section 274(d) apply to an employee even if the requirements of section 274 do not apply to the employee's employer for deduction purposes (such as when the employer is a tax-exempt organization or a governmental unit).

Section 1.132-5(c)(2) of the regulations provides that the substantiation requirements of section 274(d) are satisfied by "adequate records or sufficient evidence corroborating the [employee's] own statement." Therefore, such records or evidence provided by the employee, and relied upon by the employer to the extent permitted by the regulations promulgated under section 274(d), will be sufficient to substantiate a working condition fringe exclusion.

Section 1.61-21(a)(4)(i) of the regulations provides that a taxable fringe benefit is included in the income of the person performing the services in connection with which the fringe benefit is furnished. Thus, a fringe benefit may be taxable to a person even though that person did not actually receive the fringe benefit. If a fringe benefit is furnished to someone other than the service provider such benefit is considered as furnished to the service provider, and use by the other person is considered use by the service provider. For example, the provision of an automobile by an employer to an employee's spouse in connection with the performance of services by the employee is taxable to the employee. The automobile is considered available to the employee and use by the employee's spouse is considered use by the employee.

Section 1.61-21(b)(6)(i) of the regulations provides that if the non-commercial flight special valuation rule of section 1.61-21(g) does not apply, the value of a flight on an employer-provided piloted aircraft is determined under the general valuation principles set forth in this paragraph. Section 1.61-21(b)(6)(ii) of the regulations provides that if an employee takes a flight on an employer-provided piloted aircraft and that employee's flight is primarily personal (see section 1.162-2(b)(2)), the value of the flight is equal to the amount that an individual would have to pay in an arm's-length transaction to charter the same or a comparable piloted aircraft for that period for the same or a comparable flight. A flight taken under these circumstances may not be valued by reference to the cost of commercial airfare for the same or a comparable flight.

The cost to charter the aircraft must be allocated among all employees on board the aircraft based on all the facts and circumstances unless one or more of the employees controlled the use of the aircraft. Where one or more employees control the use of the aircraft, the value of the flight shall be allocated solely among such controlling employees, unless a written agreement among all the employees on the flight otherwise allocates the value of such flight. Notwithstanding the allocation required by the preceding sentence, no additional amount shall be included in the income of any employee whose flight is properly valued under the special valuation rule of section 1.61-21(g). For purposes of this paragraph, "control" means the ability of the employee to determine the route, departure time and destination of the flight. The rules provided in section 1.61-21(g)(3) will be used for purposes of this section in defining a flight. Notwithstanding the allocation required by the preceding sentence, no additional amount shall be included in the income of an employee for that portion of any such flight which is excludable from income pursuant to section 132(d) of the Code or section 1.132-5 of the regulations as a working condition fringe.

Section 1.61-21(g)(1) of the regulations provides that under the non-commercial flight valuation rule, except as provided in the seating capacity rule of section 1.61-21(g)(12), if an employee is provided with a flight on an employer-provided aircraft, the value of the flight is calculated using the aircraft valuation formula of section 1.61-21(g)(5).

Section 1.61-21(g)(2) of the regulations provides that the non-commercial flight valuation rule may be used to value flights on all employer-provided aircraft, including helicopters. The non-commercial flight valuation rule may be used to value international as well as domestic flights. The non-commercial flight valuation rule may not be used to value a flight on any commercial aircraft on which air transportation is sold to the public on a per-seat basis.

Section 1.61-21(g)(4) of the regulations provides that the non-commercial flight valuation rule applies to personal flights on employer-provided aircraft. A personal flight is one the value of which is not excludable under another income tax section, such as section 132(d)(relating to a working condition fringe). If an employee combines, in one trip, personal and business flights on an employer-provided aircraft and the employee's trip is primarily for the employer's business (see section 1.162-2(b)(2)), the employee must include in income the excess of the value of all the flights that comprise the trip over the value of the flights that would have been taken had there been no personal flights but only business flights. If an

employee combines, in one trip, personal and business flights on an employer-provided aircraft and the employee's trip is primarily personal, the amount includible in the employee's income is the value of the personal flights that would have been taken had there been no business flights but only personal flights.

Section 1.162-2(b)(2) of the regulations provides that whether a trip is related primarily to the taxpayer's trade or business or is primarily personal in nature depends on the facts and circumstances in each case. The amount of time during the period of the trip which is spent on personal activity compared to the amount of time spent on activities directly relating to the taxpayer's trade or business is an important factor in determining whether the trip is primarily personal. If, for example, a taxpayer spends one week while at a destination on activities which are directly related to his trade or business and subsequently spends an additional five weeks for vacation or other personal activities, the trip will be considered primarily personal in nature in the absence of a clear showing to the contrary.

Section 1.61-21(g)(5) of the regulations provides that under the non-commercial flight valuation rule, the value of a flight is determined under the base aircraft valuation formula (also known as the Standard Industry Fare Level formula or SIFL) by multiplying the SIFL cents-per-mile rates applicable for the period during which the flight was taken by the appropriate aircraft multiple, as provided, and then adding the applicable terminal charge. Under section 1.61-21(g)(7), the aircraft multiples are based on the maximum certified takeoff weight of the aircraft. The aircraft multiples also depend on whether the employee is a "control employee."

Section 1.61-21(g)(9) of the regulations provides, in part, that a control employee of a government employer includes any elected official.

Section 1.132-5(m)(4) of the regulations provides that if, for a bona fide business-oriented security concern, the employer requires that an employee travel on an employer-provided aircraft for a personal trip, the employer and the employee may exclude from the employee's gross income, as a working condition fringe, the excess value of the aircraft trip over the safe harbor airfare without having to show what method of transportation the employee would have flown but for the bona fide business-oriented security concern. For purposes of the safe harbor rule of this paragraph (m)(4), the value of the safe harbor airfare is determined under the non-commercial flight valuation rule of section 1.61-21(g) (regardless of whether the employer or

employee elects to use such valuation rule) by multiplying an aircraft multiple of 200-percent by the applicable cents-per-mile rates and the number of miles in the flight and then adding the applicable terminal charge. The value of the safe harbor airfare determined under this paragraph (m)(4) must be included in the employee's income (to the extent not reimbursed by the employee) regardless of whether the employee or the employer uses the special valuation rule of § 1.61-21(g). The excess of the value of the aircraft trip over this amount may be excluded from gross income as a working condition fringe. If, for a bona fide business-oriented security concern, the employer requires that an employee's spouse and dependents travel on an employer-provided aircraft for a personal trip, the special rule of this paragraph (m)(4) is available to exclude the excess value of the aircraft trips over the safe harbor airfares.

In 1974, the Joint Committee on Internal Revenue Taxation considered the issue of the taxation of personal use of government aircraft by then-President Nixon and his family and friends.[1] In the Nixon Report, at page 163, the Joint Committee stated that, "The staff believes that the personal use of Government airplanes by the President's family and friends should be classified as income to him for income tax purposes." The Committee went on to state that,

> One question involves the issue of whether there should be an inclusion in income of any amount with respect to the President's own use of Government aircraft. Some of his use could be classified as primarily personal since the flights take him to locations where he spends a significant part of his time on vacation. However, it is also pointed out that the President, by the nature of the office, must hold himself available for work at virtually any time. In part because of this characteristic of the Presidency and in part because of the uncertain status of such items in the past, the staff is not recommending that any amounts be included in income with respect to personal transportation of the President. In making this recommendation, the staff is not suggesting that this be foreclosed as a possible issue in the future.

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[1] Joint Committee on Internal Revenue Taxation, Examination of President Nixon's Tax returns for 1969-1972, S. Rep. No. 93-768, 93rd Cong., 2d Sess. (April 3, 1974) (hereinafter, the Nixon Report). This report, of course, predated the enactment in 1984 of section 132 of the Code and the subsequent issuance of the fringe benefit regulations.

SUMMARY

Based on the foregoing authorities, and the limited factual background at our disposal, we have reached the following conclusions.

1. If adequate records are not maintained in accordance with the requirements of section 274(d), the total value of all the flights taken by the Governor on state-provided aircraft (including helicopters) must be included in the gross income of the Governor. Even though some of the trips may have been primarily business in nature, section 1.132-5(c)(1) of the regulations prohibits an exclusion from gross income when the substantiation requirements of section 274(d) are not met.

If adequate records are maintained that meet the substantiation requirements of section 274(d), then the remaining issues are twofold. First, what portion of the value of the flights is excludable as a working condition fringe? Second, if the value of a flight is includible in income, what is the proper method for valuing that flight?

2. Whether the Governor qualifies for a working condition fringe exclusion depends upon the extent that, if he had paid for such helicopter or other aircraft trip himself, he would be allowed to deduct the expense under section 162. Under section 1.162-2(b)(2) of the regulations, the determination as to whether a trip is related primarily to the taxpayer's trade or business or is primarily personal in nature depends on the facts and circumstances in each case. An important factor to consider is the amount of time during the period of the trip which is spent on personal activity compared to the amount of time spent on activities directly relating to the business of state government.

As pointed out in the Nixon Report, by the nature of the office, the President of the United States must hold himself available for work at virtually any time. While state governors do not have the same functions as the President, especially with regard to national security functions and the duties of Commander in Chief of the Armed Forces, the character of the position of Governor is one factor to be considered in making a factual determination on whether a trip is primarily business or personal in nature. However, there is no presumption that all travel by a governor is always business in nature. For example, the mere fact that the Governor may receive some business-related phone calls while on vacation does not serve to convert an otherwise personal trip into a deductible business trip. On the other hand, if most of the time on the trip is spent on activities directly relating to the business of state government, the trip may be primarily related to the trade or business of state

government even though some small amount of time may have been devoted to personal activities.

3. With respect to valuation of the trips that are includible in gross income, the general valuation rule of section 1.61-21(b)(6) could be used to include in income the amount that an individual would have to pay in an arm's-length transaction to charter the same or a comparable piloted aircraft for that period for the same or a comparable flight.

Alternatively, provided that adequate records are maintained, the Governor may qualify for use of the non-commercial flight valuation rule of section 1.61-21(g) of the regulations (the SIFL valuation formula) by multiplying the SIFL cents-per-mile rates applicable for the period during which the flight was taken by the appropriate aircraft multiple, as provided, and then adding the applicable terminal charge. Because the Governor is an elected official, he is a "control employee" as that term is defined in section 1.61-21(g)(9) of the regulations, and the SIFL formula would be applied using the aircraft multiple for a control employee.

We were not provided any information that would indicate that the state requires that the Governor travel on a state-provided aircraft for personal trips because of a bona fide business-oriented security concern. Therefore, it does not appear that the Governor would qualify to use the safe harbor airfare of section 1.132-5(m)(4) of the regulations (i.e., by multiplying an aircraft multiple of 200-percent by the applicable cents-per-mile rates and the number of miles in the flight and then adding the applicable terminal charge).

We hope that this information will prove helpful to you. If you have any additional questions regarding this issue, please call Richard Pavel at (202) 566-3503.

By_____
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